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TNPSC GROUP I MAIN - 2021
MANDATORY TEST XVIII
PAPER III – UNIT III INDIAN ECONOMY - CURRENT ECONOMIC TRENDS AND IMPACT OF GLOBAL ECONOMY ON INDIA - II

Time: 3 hours **Total marks: 250**

SECTION A **10 x 10 = 100**

Answer all the questions. Answer not exceeding 150 words each

1. Discuss the factors responsible for nationalisation of commercial banks in India
இந்தியாவில் வணிக வங்கிகளை தேசியமயமாக்குவதற்கான காரணிகள் பற்றி விவாதி

Nationalisation of Banks

There were nearly 600 banks with 4800 branches in the country though these private sector banks were functioning fairly well, they had their problems as well and also several drawbacks. They were criticised as being non-responsive. **July 19, 1969** is a historic day in Indian banking, as a momentous and bold step was taken by the government of India. By the ordinance promulgated on that day, **14 major commercial banks** of India with deposits of **50 crores** or more were nationalised.

On **April 15, 1980 six** more commercial banks were nationalised, as the total deposits of these banks exceeded Rs. **200 crores** each. These 20 banks and the state Bank of India and its 7 associate banks which were already nationalised, constitute 28 banks in the public sector. The Regional Rural Banks throughout the country are sponsored by the Public sector banks. Thus the public sector controls practically the whole banking industry.

COMMERCIAL BANK

The following factors were responsible for nationalisation of commercial banks in 1969.

(i) ***Private ownership of commercial banks and concentration of economic power:*** Until nationalization, all major banks were controlled by one or more business houses. These business houses used the resources contributed by the mass of the people for their own personal benefits. They financed those projects which ultimately enhanced their own financial resources. Thus, private ownership of banks resulted in concentration of income and wealth in few hands.

(ii) ***Urban-bias:*** Prior to nationalization, commercial banks had shown no interest in establishing offices in semi-urban and rural areas. More and more branches were opened in cities resulting in concentration of banking facilities in urban

areas. For example, out of about 5.6 lakh villages in India, only 500,0 were being served by commercial banks and five major cities (Ahmedabad, Bombay, Calcutta, Delhi and Madras) together had one-seventh share in the number of bank offices and about fifty percent share of bank deposits and bank credit. This urban biased nature of commercial banks led to slow rate of growth in the rural areas.

(iii) *Neglect of agricultural sector*: There was a total neglect of the agricultural sector and its finance prior to nationalization of banks.- The banks increasingly advanced finances to commerce and industry with the result their share in the scheduled banks advances increased from 70 per cent in 1951 to 87 per cent in!968. Agriculture accounted for only 2.2 per cent of the total advances.

(iv) *Violation of norms*: Commercial banks often violated the norms and priorities laid down in the plans and granted loans to even those industries which figured nowhere in the priority list.

(v) *Speculative activities*: Private commercial banks earned large profits and indulged in speculative activities. They even extended advances to hoarders and black marketers against high rates of interest.

2. Explain the role of NBFI in Indian Economy
இந்திய பொருளாதாரத்தில் வங்கி சாராத நிதி நிறுவனங்களின் பங்கு பற்றி விளக்குக

NBFIs.

Non-Banking Financial Companies classified under NBFI (Non-banking financial intermediaries) are those which are also doing the similar functions of banks but are not coming under the Banking Companies Act. They accept deposits from the public and also give loan to the public for various purposes. The main difference between NBFCs and the bank is that the deposits, with NBFCs cannot be withdrawn on demand, except after the expiry of a fixed period. They also come under the control of Reserve Bank of India.

The non-banking financial companies are brought under the control of RBI by separate set of rules and regulations. The non -banking non-financial companies are nothing but joint stock companies which accept deposits from the public subject to the limitations of the Companies Act, 1956.

NBFCs consist of

1. Chit funds

2. Nidhis

3. Benefit society

4. Finance Company

5. Factoring

6. Leasing

7. Hire purchase finance companies

3. Enlist the functions of SEBI.
SEBI -யின் பணிகளை பட்டியலிடுக.

Functions of SEBI

Securities and Exchange Board of India (frequently abbreviated SEBI) is the nodal agency which safeguards the interests of an investor in the Indian Financial market. SEBI performs three key functions: quasi-legislative, quasi-judicial and quasi-executive. It drafts regulations, conducts investigation & enforcement action and it passes rulings and orders.

i. Safeguarding the interests of investors by means of adequate education and guidance. SEBI makes rules and regulation that must be followed by the financial intermediaries like portfolio exchanges, underwriters and merchant bankers, etc. It takes care of the complaints received from investors . Additionally, it issues notices and booklets for the information, assistance and protection of small investors.
ii. Regulating and controlling the business on stock markets. Registration of brokers and sub-brokers is made mandatory and they have to abide by certain regulations and rules.
iii. Conduct inspection and inquiries of stock exchanges, intermediaries and self-regulating organizations and to take appropriate measures wherever required. This function is carried out for organized working of stock exchanges and intermediaries.
iv. Barring insider trading in securities.
v. Prohibiting deceptive and unfair methods used by financial intermediaries operating in securities markets.
vi. Registering and controlling the functioning of stock brokers, sub-brokers, share transfer agents, bankers, trustees, registrars, merchant bankers, underwriters, portfolio managers, investment advisers and various other intermediaries who might be linked to securities markets in any manner.
vii. SEBI issues Guidelines and Instructions to businesses concerning capital issues Separate guidelines are provided for initial public issue made by listed companies, etc. It conducts research and publishes information beneficial to all market players (i.e. all buyers and sellers).
viii. SEBI regulates mergers and acquisitions as a way to protect the interest of investors. For this, SEBI has released appropriate guidelines with the intention that such mergers and takeovers won't be at the expense of small investors.
ix. Registering and controlling the functioning of collective investment schemes such as mutual funds. SEBI has created regulations and guidelines that should be followed by mutual funds. The aim is to maintain effective supervision and avoid any unfair and anti-investor actions.
x. Promoting self-regulatory organization of intermediaries. It has extensive legal powers. Having said that, self-regulation is preferable to external regulation. The function of SEBI is to motivate financial intermediaries to create their professional associations and manage harmful actions of their members. It can also make use of its powers when needed for protection of investors.

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xi. Carrying out steps in order to develop the capital markets by having an accommodating approach.

xii. Provide appropriate training to financial intermediaries. This function is great for healthy environment in the stock markets and also for the protection of investors.

xiii. Levying fee or any other type of charges to carry out the purpose of the Act.

xiv. Performing functions that may be assigned to it by the Central Government of India

4. List out the recommendations of Narasimhan Committee on Financial Sector Reforms
நிதித்துறை சீர்த்திருத்தங்கள் மீதான நரசிம்மன் குழுவின் பரிந்துரைகளை பட்டியலிடுக

Recommendations of Narasimhan Committee on Financial System

- The recommendations the Committee on the Financial System chaired by M.Narasimhan, former Governor of Reserve Bank of India are worth mentioning in the context of improving the working of commercial banks. The committee presented its report in December 1991 and its recommendations cover a wide spectrum of public sector banks, financial institutions and also capital market. Some of the significant recommendations relating to banks are briefed as follows:

1. **New Banking Structure Proposed:** The Committee recommended some basic changes in the banking structure. The pattern should be:
   a) Three or four large banks (including State Bank of India) which could be international in character;
   b) About 10 national banks with a network o0f branches throughout the country could be engaged in universal banking;
   c) Local Banks with functions to specific regions of the country; and
   d) Rural Banks including Regional Rural Bank whose operations could be confined to rural areas only and allied business will be primarily and predominantly in financing agriculture and allied activities. Thus, a restructure of banks on four-tier system has been proposed.

2. **Enhancement of Capital base of the Banks:** The Committee suggested that the banks should be allowed to raise fresh capital from the public as inadequacy of capital becomes a cause of concern among banks. According to the Committee, the capital adequacy ratio in relation to risk weighted assets should be 8 per cent by March 1996, as it was only 2 per cent at the time of presenting the recommendations.

3. **Deregulation of interest rates:** The Committee recommended deregulation of interest on loans in order to make them reflect market conditions. It also proposed that interest rate on government borrowings should be closer to market-determined rate. However, the interest rates on bank deposits may continue to be regulated.

4. **Recovery of Bad debts and Tribunals:** Banks experience lot of difficulties in the recovery of loans and the overdues are mounting up. The Committee suggested that Special Tribunals should be set up to speed up the process of recovery of debts. Further, the Committee recommended the setting up of Asset Reconstruction Fund (ARF) which could take over from the banks and financial institutions, a portion of the bad debts and doubtful debts at a discount, and recover the same from the borrowers. The Committee also suggested that the banks should follow uniform

accounting practices which should include non-recognition of income from non-performing assets, and provision against different types of debts.

5. **Cut in S.**L.R. **and C.R.R:** The Committee recommended to cut down Statutory Liquidity Ratio in phased manner to 25% over a period of five year from 1991. The Committee also recommended that the RBI should progressively reduce cash Reserve Ratio from its present high level.

6. **End of Dual Control & Functional Autonomy:** The committee suggested that the duality of control by Banking Division of Ministry of Finance and leaving the latter (i.e., RBI) to regulate the Banking system. The committee recommended functional autonomy of public sector banks; and this should be ensured by injecting 'competition' in the financial sector so as to marketwise the functioning of the banks.

7. **Liberalization of Capital Market:** The Committee strongly favoured dispensation of prior approval of any issue by the Government or Securities Exchange Board of India (SEBI). The issuing company should be free to decide on the nature of shares and bonds, their terms and pricing. Further, the capital market should be gradually opened up for Foreign Portfolio Investment.

8. **Abolition of Branch Licensing:** The committee recommended abolition of branch licensing and the opening or closing of branches should be left to the discretion of the individual banks. This will not apply to rural branches.

9. **Appointment and recruitments:** The Committee strongly believes that in the matters of appointment of the Chief Executives of the banks and members of the Board of Banks, professionalism and integrity should be prime considerations.

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5. Who release Financial stability report? Bring out the important features of 22nd Financial stability Report

நிதிநிலைத்தன்மை அறிக்கையை வெளியிடுவது யார்? 22வது நிதி நிலைத்தன்மை அறிக்கையின் முக்கிய அம்சங்களை வெளிக்கொணர்க

FINANCIAL STABILITY

The Reserve Bank released the 22nd issue of the Financial Stability Report (FSR), which reflects the collective assessment of the Sub-Committee of the Financial Stability and Development Council (FSDC) on risks to financial stability, and the resilience of the financial system in the context of contemporaneous issues relating to development and regulation of the financial sector. The release of FSR was rescheduled to incorporate the first advance estimates of national income for 2020-21 that were released by the National Statistical Office on January 7, 2021.

Highlights:

- In the initial phase of the COVID-19 pandemic, policy actions were geared towards restoring normal functioning and mitigating stress; the focus is now being oriented towards supporting the recovery and preserving the solvency of businesses and households.
- Positive news on vaccine development has underpinned optimism on the outlook, though it is marred by second wave of the virus including more virulent strains.

- Policy measures by the regulators and the government have ensured the smooth functioning of domestic markets and financial institutions; managing market volatility amidst rising spill overs has become challenging especially when the movements in certain segments of the financial markets are not in sync with developments in the real sector.
- Bank credit growth has remained subdued, with the moderation being broad-based across bank groups.
- Performance parameters of banks have improved significantly, aided by regulatory dispensations extended in response to the COVID-19 pandemic.
- The capital to risk-weighted assets ratio (CRAR) of Scheduled Commercial Banks (SCBs) improved to 15.8 per cent in September 2020 from 14.7 per cent in March 2020, while their gross non-performing asset (GNPA) ratio declined to 7.5 per cent from 8.4 per cent, and the provision coverage ratio (PCR) improved to 72.4 per cent from 66.2 per cent over this period.
- Macro stress tests incorporating the first advance estimates of gross domestic product (GDP) for 2020-21 released on January 7, 2021 indicate that the GNPA ratio of all SCBs may increase from 7.5 per cent in September 2020 to 13.5 per cent by September 2021 under the baseline scenario; the ratio may escalate to 14.8 per cent under a severe stress scenario. This highlights the need for proactive building up of adequate capital to withstand possible asset quality deterioration.
- Network analysis reveals that total bilateral exposures among entities in the financial system increased marginally during the quarter-ended September 2020. With the inter-bank market continuing to shrink and with better capitalisation of banks, the contagion risk to the banking system under various scenarios declined as compared to March 2020.

6. Explain the role of NABARD in agricultural credit
விவசாயக் கடனில் நபார்டின் பங்கு பற்றி விளக்குக

With the establishment of *National Bank for Agriculture and Rural Development* (NABARD), all the functions of the RBI relating to agricultural credit had been taken over and looked after by NABARD since 1982. Since then, all activities relating to rural credit are entirely looked after by NABARD.

NABARD and its role in Agricultural credit

Since its inception, RBI has shown keen interest in agricultural credit and maintained a separate department for this purpose. RBI extended short-term seasonal credit as well as medium-term and long-term credit to agriculture through State level co-operative banks and Land Development banks.

At the same time, RBI has also set up the Agricultural Refinance Development Corporation (ARDC) to provide refinance support to the banks to promote programmes of agricultural development, particularly those requiring term credit. With the widening of the role of bank credit from "agricultural development" to "rural development" the Government proposed to have a more broad-based organization at the apex level to extend support and give guidance to credit institutions in matters relating to the formulation and implementation of rural development programmes.

A National Bank for Agriculture and Rural Development (NABARD), was therefore, set up in July 1982 by an Act of parliament to take over the functions of ARDC and the refinancing functions of RBI in relation to co-operative banks and RRBs. NABARD is linked

organically with the RBI by the latter contributing half of its share capital the other half being contributed by the Government of India (GOI). GOI nominates three of its Central Board Directors on the board of NABARD.A Deputy Governor of RBI is appointed as Chairman of NABARD.

Functions of NABARD

NABARD has inherited its apex role from RBI i.e, it is performing all the functions performed by RBI with regard to agricultural credit.

(i) NABARD acts as a refinancing institution for all kinds of production and investment credit to agriculture, small-scale industries, cottage and village industries, handicrafts and rural crafts and real artisans and other allied economic activities with a view to promoting integrated rural development.

(ii) It provides short-term, medium-term and long-term credits to state co-operative Banks (SCBs), RRBs, LDBs and other financial institutions approved by RBI.

(iii) NABARD gives long-term loans (upto 20 Years) to State Government to enable them to subscribe to the share capital of co-operative credit societies.

(iv) NABARD gives long-term loans to any institution approved by the Central Government or contribute to the share capital or invests in securities of any institution concerned with agriculture and rural development.

(v) NABARD has the responsibility of co-ordinating the activities of Central and State Governments, the Planning Commission (now NITI Aayog) and other all India and State level institutions entrusted with the development of small scale industries, village and cottage industries, rural crafts, industries in the tiny and decentralized sectors, etc.

(vi) It has the responsibility to inspect RRBs and co-operative banks, other than primary co-operative societies.

(vii) It maintains a Research and Development Fund to promote research in agriculture and rural development

7. What are the functions of Finance Commission? What are the effects of 80th Amendment Act (2000) of the Constitution on Finance Commission?
நிதிக்குழுவின் பணிகள் யாவை? 80-வது அரசியலமைப்பு சட்டத்திருத்தச் சட்டம் (2000) நிதிக் குழுவில் ஏற்படுத்திய விளைவுகள் யாவை?

History of Finance Commission

Finance commission is a quasi-judicial body set up under Article 280 of the Indian Constitution. It was established in the year 1951, to define the fiscal relationship framework between the Centre and the state.

Finance Commission aims to reduce the fiscal imbalances between the centre and the states (Vertical imbalance) and also between the states (horizontal imbalance). It promotes inclusiveness.

A Finance Commission is set up once in every 5 years. It is normally constituted two years before the period. It is a temporary Body.

The 14th Finance Commission was set up in 2013. Its recommendations were valid for the period from 1st April 2015 to 31st March 2020.

Article 280 of the Indian Constitution

- President after two years of the commencement of Indian Constitution and thereafter every 5 years, has to constitute a Finance Commission of India.
- It shall be the duty of the Commission to make recommendations to the President in relation to the:
- the distribution between the Union and the States of the net proceeds of taxes which are to be, or maybe, divided between them and the allocation between the States of the respective shares of such proceeds;
- the principles which should govern the grants in aid of the revenues of the States out of the Consolidated Fund of India; any other matter referred to the Commission by the President in the interests of sound finance
- The Commission shall determine their procedure and shall have such powers in the performance of their functions as Parliament may by law confer on them

The Constitution (80th Amendment) Act, 2000

- Based on the recommendations of the Tenth Finance Commission, an alternative scheme for sharing taxes between the Union and the State has been enacted by the Constitution (Eightieth Amendment) Act, 2000.
- Under the new scheme of devolution of revenue between Union and the States, 26 per cent out of gross proceeds of Union taxes and duties is to be assigned to the States in lieu of their existing share in the income-tax, excise duties special excise duties and grants in lieu of tax on railway passenger fares.

8. What are the impact and challenges of Globalization?
உலகமயமாக்கலின் விளைவுகள் மற்றும் அதில் உள்ள சவால்கள் யாவை?

Impact and Challenges of Globalization

Positive Impact

- A better economy introduces rapid development of the capital market.
- Standard of living has increased.
- Globalization rapidly increases better trade so that more people are employed.
- Introduced new technologies and new scientific research patterns.
- Globalization increasing the GDP of a country.
- It helps to increase in free flow of goods and also to increase Foreign Direct Investment.

Negative Impact

- Too much flow of capital amongst countries, Introduces unfair and immoral distributors of Income.

- Another fear is losing national integrity. Because of too much exchange of trade, independent domestic policies are lost.
- Rapid growth of the economy has required a major infrastructure and resource extraction. This increase negative ecological and Social costs.
- Rapid increases in exploitation of natural resources to earn foreign exchange.
- Environmental standards and regulations have been relaxed.

Challenges of Globalization

- The benefits of globalization extend to all countries that will not happen automatically.
- The fear that globalization leads to instability in the developing world.
- The industrial world that increased global competition will lead in race to the bottom in wages, labour right, and employment practice.
- It leads to global inbalance.
- Globalization has resulted with the embarrassment.
- Globalization has led to an increase in activities such as child labor and slavery.
- People started consuming more junk food. This caused, the degradation of health and spread of diseases.
- Globalization has led to environmental degradation.

9. What do you mean by demonetization? Briefly describe the economic consequences of demonetization in India.
பணமதிப்பு நீக்கம் என்றால் என்ன? இந்தியாவில் பணமதிப்பு நீக்கத்தினால் ஏற்படும் பொருளாதார விளைவுகளை சுருக்கமாக விளக்குக.

Meaning of Demonetization

Demonetization is the withdrawal of a particular form of currency from circulation. It is a process by which a series of currency will not be legal tender. The series of currency, which w not be legal tender, will not accept as valid currency. In other words, it is the act of stripping i currency unit of its status as legal tender. Demonetization is necessary whenever there is a change of national currency. The old unit of currency must be retired and replaced with a new currency.

The Government's Actions

The actions taken by the Government of India towards demonetization are as follows:

1. The Government has decided to replace the existing set of ì 500 currency notes and completely abolish the ₹ 1000 denomination. PM Modi announced that the RBI will introduce ₹ 2000 as a new denomination in India.
2. The move is intended to fight corruption, black money and money laundering. In short the idea. is to bring the parallel economy to a halt. And divert as much as possible to the banking system.
3. Currently ₹ 17,54,000 crore worth of notes are in circulation according to the RBI's database on the Indian economy. Of this ₹ 500 notes constituted almost 45% of the currency in circulation while 39% of the notes were of the ì 1000 denomination.

We have assumed 30% of the cash floating in the economy would be undeclared income. Please note that exact cash flows (Amount of legitimate and illegitimate money) would be determined post March 2017 once the window for depositing old notes of ases,

Economic Consequences of Demonetization of 500 And 1000 Rupees Notes

The economic consequences of demonetization are described here in below:

1. **Effect on Parallel Economy**: The removal ₹ 500 and ₹ 1000 notes and replacement of the same with new ₹ 500 and ₹ 2000 Rupees notes is expected to- (i) remove black money from the economy as they will be blocked since the owners will not be in a position to deposit the same in the banks, to temporarily stall the circulation of large volume of counterfeit currency, and (ii) curb the funding for anti-social elements like smuggling, terrorism, espionage, etc.

2. **Effect on Money Supply**: With the older 500 and 1000 Rupees notes being scrapped, until the new 500 and 2000 Rupees notes get widely circulated in the market, money supply is expected to reduce in the short run. To the extent that black money (which is not counterfeit) does not re-enter the system, reserve money and hence money supply will decrease permanently. However gradually as the new notes get circulated in the market and the mismatch gets corrected, money supply will pick up.

3. **Effect on Demand**: The overall demand is expected to be affected to an extent. The demand in following areas is to be impacted particularly: Consumer goods, Real Estate and Property, Gold and luxury goods and Automobiles (only to a certain limit). All these mentioned sectors are expected to face certain moderation in demand from the consumer side, owing to the significant amount of cash transactions involved in these sectors.

4. **Effect on Prices**: Price level is expected to be lowered due to moderation from demand side. Consumer goods' prices are expected to fall only marginally due to moderation in demand as use of cards and cheques would compensate for some purchases. Real estate and property prices are largely expected to fall, especially for sales of properties where major part of the transaction is cash based, rather than based on banks transfer or cheque transactions. In the medium term, however the prices in this sector could regain some levels as developers rebalance their prices (probably charging more on cheque payment).

5. **Effect on Various Economic Entities**: As cash transaction lowering in the short run, till the new notes are spread widely into circulation, certain sections of the society could face short term disruptions in facilitation of their transactions. These sections are as below
    a. Agriculture and related sector.
    b. Small traders.
    c. SME.
    d. Services Sector.
    e. Households.
    f. Political Parties.
    g. Professionals like doctor, carpenter, utility service providers, etc.
    h. Retail outlets.

The nature, frequency and amounts of the commercial transactions involved with these sections of the economy necessitate cash transactions on more frequent basis. Thus, these segments are expected to have the most significant impact post this demonetization process and the introduction of new notes in circulation.

6. **Effect on GDP**: The GDP formation could be impacted by this measure, with reduction in the consumption demand. However this expected impact on GDP may not be significant as some of this demand will only be deferred and re-enter the stream once the cash situation becomes normal.

7. **Effect on Banks**: As directed by the Government, 500 and 1000 Rupees notes, which now cease to be legal tender, are to be deposited or exchanged in banks (subject to certain limits). This will automatically lead to more amounts being deposited in Savings and Current Account of commercial banks. This in turn will enhance the liquidity position of the banks, which, can be utilized further for lending purposes. However, to the extent that households have held on to these funds for emergency purposes, there would be withdrawals at the second stage.

8. **Effect on Online Transactions and Alternative Modes of Payment**: With cash transactions facing a reduction, alternative forms of payment will see a surge in demand. Digital transaction systems, E wallets and apps, online transactions using E banking, usage of Plastic money (Debit and Credit Cards), etc. will definitely see substantial increase in demand. This should eventually lead to strengthening of such systems and the infrastructure required.

9. **Economist's View**: In spite of the initial hiccups and disruptions in the system, eventually this change will be well assimilated and will prove positive for the economy in the long run. Black money hoarders will definitely lose out, eventually boosting the formal economy in the long run. Short term fall in real estate prices might benefit middle class citizens. This move by the Government along with the implementation of the GST will eventually make the system more accountable and efficient.

10. Explain the objectives of fiscal policy.
நிதிக்கொள்கையின் நோக்கங்களை விவரி.

Objectives of Fiscal Policy:

The Fiscal Policy is useful to achieve the following objectives:

1. Full Employment

Full Employment is the common objective of fiscal policy in both developed and developing countries. Public expenditure on social overheads help to create employment opportunities. In India, public expenditure on rural employment programmes like MGNREGS is aimed at employment generation.

2. Price Stability

Price instability is caused by mismatch between aggregate demand and aggregate supply. Inflation is due to excess demand for goods. If excess demand is

caused by Government expenditure in excess of real output, the most effective measure is to cut down public expenditure. Taxation of income is the best measure if excess demand is due to private spending. Taxation reduces disposable income and so aggregate demand.

To fight depression, the Government needs to increase its spending and reduce taxation.

3. **Economic Growth**

Fiscal Policy is used to increase the productive capacity of the economy. Tax is to be used as an instrument for encouraging investment. Tax holidays and tax rebates for new industries stimulate investment. Public sector investments are to be increased to fill the gap left by private investment. When resource mobilization through tax measures is inadequate, the Government resorts to borrowing both from internal and external sources to finance growth projects.

4. **Equitable distribution**

Progressive rates in taxation help to reduce the gap between rich and poor. Similarly progressive rates in public expenditure through welfare schemes such as free education, noon meal for school children and subsidies promote the living standard of poor people.

5. **Exchange Stability**

Fluctuations in international trade cause movements in exchange rate. Tax concessions and subsidy to export oriented units help to boost exports. Customs duties on import of non-essential items help to cut import bill. The reduction in import duty on import of raw material and machinery enables reduction in cost and make the exports competitive.

6. **Capital formation**

Capital formation is essential for rapid economic development. Tax relief helps to increase disposable income, savings and thereby capital formation. Government expenditure on infrastructure development like power and transport encourages private investment.

7. **Regional balance**

Fiscal incentives for industries in the backward regions help to narrow down regional imbalances. Public expenditure may be used to start industrial estates so that industrial activity is stimulated in backward regions.

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SECTION – B **10 x 15 = 150**

Answer all the questions. Answer not exceeding 250 words each

11. What are the objectives of monetary policy? Explain the Credit Control Methods of RBI
பணக்கொள்கையின் நோக்கங்கள் யாவை? இந்திய ரிசர்வ் வங்கியின் கடன் கட்டுப்பாட்டு முறைகள் பற்றி விளக்குக

Objectives of Monetary Policy

The monetary policy in developed economies has to serve the function of stabilization and maintaining proper equilibrium in the economic system. But in case of underdeveloped countries, the monetary policy has to be more dynamic so as to meet the requirements of an expanding economy by creating suitable conditions for economic progress. It is now widely recognized that monetary policy can be a powerful tool of economic transformation.

1. **Neutrality of Money**
2. **Exchange Rate Stability**
3. **Price Stability**
4. **Full Employment**
5. **Economic Growth**
6. **Equilibrium in the Balance of Payments**

Methods of Credit Control

I. Quantitative or General Methods:

1. **Bank Rate Policy:**

The bank rate is the rate at which the Central Bank of a country is prepared to re-discount the first-class securities. It means the bank is prepared to advance loans on approved securities to its member banks. As the Central Bank is only the lender of the last resort the bank rate is normally higher than the market rate. For example: If the Central Bank wants to control credit, it will raise the bank rate. As a result, the deposit rate and other lending rates in the money-market will go up. Borrowing will be discouraged, and will lead to contraction of credit and vice versa.

2. **Open Market Operations:**

In narrow sense, the Central Bank starts the purchase and sale of Government securities in the money market.

In Broad Sense, the Central Bank purchases and sells not only Government securities but also other proper eligible securities like bills and securities of private concerns. When the banks and the private individuals purchase these securities they have to make payments for these securities to the Central Bank.

3. Variable Reserve Ratio:

(a) Cash Reserves Ratio:

Under this system the Central Bank controls credit by changing the Cash Reserves Ratio. For example, if the Commercial Banks have excessive cash reserves on the basis of which they are creating too much of credit, this will be harmful for the larger interest of the economy. So it will raise the cash reserve ratio which the Commercial Banks are required to maintain with the Central Bank.

Similarly, when the Central Bank desires that the Commercial Banks should increase the volume of credit in order to bring about an economic revival in the economy. The central Bank will lower down the Cash Reserve Ratio with a view to expand the lending capacity of the Commercial Banks.

Variable Cash Reserve Ratio as an objective of monetary policy was first suggested by J.M. Keynes. It was first followed by Federal Reserve System in United States of America. The commercial banks as per the statute has to maintain reserves based on their demand deposit and fixed deposit with central bank is called as Cash Reserve Ratio.

If the CRR is high, the commercial bank's capacity to create credit will be less and if the CRR is low, the commercial bank's capacity to create credit will be high.

(b) **Statutory Liquidity Ratio:**

Statutory Liquidity Ratio (SLR) is the amount which a bank has to maintain in the form of cash, gold or approved securities. The quantum is specified as some percentage of the total demand and time liabilities (i.e., the liabilities of the bank which are payable on demand anytime, and those liabilities which are accruing in one month's time due to maturity) of a bank.

II. Qualitative or Selective Method of Credit Control:

The qualitative or the selective methods are directed towards the diversion of credit into particular uses or channels in the economy. Their objective is mainly to control and regulate the flow of credit into particular industries or businesses. The following are the frequent methods of credit control under selective method:

1. Rationing of Credit
2. Direct Action
3. Moral Persuasion
4. Method of Publicity
5. Regulation of Consumer's Credit
6. Regulating the Marginal Requirements on Security Loans

1. **Rationing of Credit**

This is the oldest method of credit control. Rationing of credit as an instrument of credit control was first used by the Bank of England by the end of the 18th Century. It aims to control and regulate the purposes for which credit is granted by commercial banks. It is generally of two types.

a) **The variable portfolio ceiling:** It refers to the system by which the central bank fixes ceiling or maximum amount of loans and advances for every commercial bank.

b) **The variable capital asset ratio:** It refers to the system by which the central bank fixes the ratio which the capital of the commercial bank should have to the total assets of the bank.

2. **Direct Action**

Direct action against the erring banks can take the following forms.

a) The central bank may refuse to altogether grant discounting facilities to such banks.

b) The central bank may refuse to sanction further financial accommodation to a bank whose existing borrowing are found to be in excess of its capital and reserves.

c) The central bank may start charging penal rate of interest on money borrowed by a bank beyond the prescribed limit.

3. **Moral Suasion**

This method is frequently adopted by the Central Bank to exercise control over the Commercial Banks. Under this method Central Bank gives advice, then requests and persuades the Commercial Banks to co-operate with the Central Bank in implementing its credit policies.

4. **Publicity**

Central Bank in order to make their policies successful, take the course of the medium of publicity. A policy can be effectively successful only when an effective public opinion is created in its favour.

5. **Regulation of Consumer's Credit:**

The down payment is raised and the number of instalments reduced for the credit sale.

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6. **Changes in the Marginal Requirements on Security Loans:**

This system is mostly followed in U.S.A. Under this system, the Board of Governors of the Federal Reserve System has been given the power to prescribe margin requirements for the purpose of preventing an excessive use of credit for stock exchange speculation.

This system is specially intended to help the Central Bank in controlling the volume of credit used for speculation in securities under the Securities Exchange Act, 1934.

12. Explain the Sources of Revenue to the Government
அரசின் வருவாய் மூலங்கள் பற்றி விளக்குக

SOURCES OF REVENUE - TAX & NON-TAX REVENUE

Public revenue occupies an important place in the study of public finance. The Government has to perform several functions for the welfare of the people. They involve substantial amount of public expenditure which can be financed only through public revenue. The amount of public revenue to be raised depends on the necessity of public expenditure and the people's ability to pay.

Meaning

The income of the government through all sources is called public income or public revenue.

According to Dalton, the term "Public Income" has two senses — wide and narrow. In its wider sense it includes all the incomes or receipts which a public authority may secure during any period of time. In its narrow sense, it includes only those sources of income of the public authority which are ordinarily known as "revenue resources." To avoid ambiguity, the former is termed "public receipts" and the latter "public revenue."

In a narrow sense, it includes only those sources of income of the Government which are described as "revenue resources". In broad sense, it includes loans raised by the Government also.

Classification of Public Revenue.

Public revenue can be classified into two types.

Tax Revenue

Meaning

Tax is a compulsory payment by the citizens to the government to meet the public expenditure. It is legally imposed by the government on the tax payer and in no case tax payer can refuse to pay taxes to the government.

Definitions

"A Tax is a compulsory payment made by a person or a firm to a government without reference to any benefit the payer may derive from the government."
-Anatol Murad

"A Tax is a compulsory contribution imposed by public authority, irrespective of the exact amount of service rendered to the tax payer in return and not imposed as a penalty for any legal offence."
- Dalton

Characteristics of Tax

i. A tax is a compulsory payment made to the government. People on whom a tax is imposed must pay the tax. Refusal to pay the tax is a punishable offence.

ii. There is no quid pro quo between a taxpayer and public authorities. This means that the tax payer cannot claim any specific benefit against the payment of a tax.

iii. Every tax involves some sacrifice on part of the tax payer.

iv. A tax is not levied as a fine or penalty for breaking law.

Some of the tax revenue sources are

- Income tax
- Corporate tax
- Sales tax
- Surcharge and
- Cess

Non-Tax Revenue

The revenue obtained by the government from sources other than tax is called Non-Tax Revenue. The sources of non-tax revenue are

1. **Fees**

   Fees are another important source of revenue for the government. A fee is charged by public authorities for rendering a service to the citizens. Unlike tax, there is no compulsion involved in case of fees. The government provides certain services and charges certain fees for them. For example, fees are charged for issuing of passports, driving licenses, etc.

2. **Fine**

   A fine is a penalty imposed on an individual for violation of law. For example, violation of traffic rules, payment of income tax after the stipulated time etc.

3. **Earnings from Public Enterprises**

The Government also gets revenue by way of surplus from public enterprises. Some of the public sector enterprises do make a good amount of profits. The profits or dividends which the government gets can be utilized for public expenditure.

4. **Special assessment of betterment levy**

It is a kind of special charge levied on certain members of the community who are beneficiaries of certain government activities or public projects. For example, due to a public park or due to the construction of a road, people in that locality may experience an appreciation in the value of their property or land.

5. **Gifts, Grants and Aids**

- A grant from one government to another is an important source of revenue in the modern days. The government at the Centre provides grants to State governments and the State governments provide grants to the local government to carry out their functions.

- Grants from foreign countries are known as Foreign Aid. Developing countries receive military aid, food aid, technological aid, etc. from other countries.

6. **Escheats**

It refers to the claim of the state to the property of persons who die without legal heirs or documented will.

The main taxes to be levied and collected by the states under the constitutions are:

i. land revenue
ii. taxes on agriculture income
iii. duties in respect of succession to agricultural land
iv. taxes on lands and buildings
v. taxes in mineral rights.
vi. duties of excise on alcoholic liquors for human consumption, medicinal and toilet preparations containing these substances.
vii. taxes on the entry of goods into a local area of consumption, use or sale therein
viii. taxes on the entry of goods into a local area of consumption, use or sale therein.
ix. taxes on the sale or purchase of goods other than newspapers.
x. taxes on advertisements published in newspaper.
xi. taxes on goods and passengers carried by road or inland water ways.
xii. taxes on vehicles animals and boats.
xiii. taxes on professions, trades and employments.
xiv. taxes on luxuries including taxes on entertainments betting and gambling.
xv. toll and
xvi. stamp duties in respect of certain types of documents.

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Non-tax revenue of the States maybe grouped under:

a. Administrative receipts from social and developmental services such as education medical and public healths, civil works etc.
b. Net Contribution of departmental undertakings comprising revenue receipts from forests, multipurpose river valley schemes electricity schemes road and water transports schemes and milk supply schemes etc.
c. Irrigation (non-commercial)
d. State raffle schemes
e. Receipts from other public undertakings such as electricity boards, road transport corporations and states investment corporations, and
f. Other miscellaneous receipts.

13. Describe the canons of Public Expenditure and canons of taxation
பொதுச்செலவு விதிகள் மற்றும் வரிவிதிப்பு விதிகளை விளக்குக

Canons of Public Expenditure

1. Canon of benefit
2. Canon of economy
3. Canon of Sanction
4. Canon of surplus
5. Canon of elasticity
6. Canon of productivity
7. Canon of equitable distribution

CANONS OF TAXATION

The characteristics or qualities which a good tax should possess are described as canons of taxation. It must be noted that canons refer to the qualities of an isolated tax and not to the tax system as a whole. A good tax system should have a proper combination of all kinds of taxes having different canons.

According to Adam Smith, there are four canons or maxims of taxation. They are as follows:

1. **Canon of Ability**

The Government should impose tax in such a way that the people have to pay taxes according to their ability. In such case a rich person should pay more tax compared to a middle class person or a poor person.

2. **Canon of Certainty**

The Government must ensure that there is no uncertainty regarding the rate of tax or the time of payment. If the Government collects taxes arbitrarily, then these will adversely affect the efficiency of the people and their working ability too.

3. **Canon of Convenience**

The method of tax collection and the timing of the tax payment should suit the convenience of the people. The Government should make convenient arrangement for all the tax payers to pay the taxes without difficulty.

4. **Canon of Economy**

The Government has to spend money for collecting taxes, for example, salaries are given to the persons who are responsible for collecting taxes. The taxes, where collection costs are more are considered as bad taxes. Hence, according to Smith, the Government should impose only those taxes whose collection costs are very less and cheap.

14. What is GST? Discuss the significance and advantages of GST
சரக்கு மற்றும் சேவை வரி என்றால் என்ன? சரக்கு மற்றும் சேவை வரியின் முக்கியத்துவம் மற்றும் நன்மைகள் பற்றி விவாதி

Goods and Services Tax (GST)

Introduction:

GST is a consumption-based tax levied on sale, manufacture and consumption of goods & services at a national level. State GST (SGST) is one, which is levied by State. Integrated GST (IGST) is levied by provide revenue for the government. The GST is paid by consumers, but it is levied and remitted to the government by businesses selling the goods and services.

Meaning & Definition of GST:

Goods & services Tax in India can be defined as "A comprehensive multi-stage, destination-based tax that will be levied on every value addition". To understand this, we need to understand the concepts under this definition. Let us start with the term "Multi-stage". Now, there are multiple steps an item goes through from manufacture or production to the final sale. Buying of raw materials is the first stage. The second stage is production or manufacture. Then, there is the warehousing of materials. The next stage is sales of the product to the retailer and in the final stage, the retailer sells to the end consumer the product completing its life cycle.

Importance of Goods and Services tax

Currently, the Indian tax structure is divided into two namely, Direct Taxes and Indirect Taxes. Direct Taxes are levies where the liability cannot be passed on to someone else. An example c: r is Income Tax where you earn me income and you alone are liable to pay the tax on it. In the case of Indirect Taxes, the liability of the tax can be passed on to someone else. This means that when the shopkeeper must pay VAT on his sale, he can pass on the liability to the customer. So, in effect, the customer pays the price of the item as well as the VAT on it so the shopkeeper can deposit the VAT to the government. This means that the customer must pay not just the price of the proc. -but he also pays the tax liability, and therefore, he has a higher outlay when he buys an item.

This happens because the shopkeeper has paid a tax when he bought the item from the wholesaler. To recover that amount, as well as to make up for the VAT he must pay to

the government, he passes the liability to the customer who has to pay the additional amount. Earlier there was no other way for the shopkeeper to recover whatever he pays from his own pocket during transaction and therefore, he had no choice but to pass on the liability to the customer. Goods and Services Tax addresses this issue. It has a system of Input Tax Credit, which is allowing sellers to claim the tax already paid, so that the final liability on the end consumer is decrease.

Operating Mechanism of GST

A nationwide tax reform cannot function without strict guidelines and provisions. The GST Council has devised a fool proof method of implementing this new tax regime by dividing it into three categories, which are as below:

1. **CGST**: Where the revenue is collected by the central government.
2. **SGST**: Where the revenue is collected by the state governments for intra-state sales.
3. **IGST**: Where the revenue is collected by the central government for inter-state sales

GST Law in India

France was the world's first country to implement GST Law in the year 1954. Since then, 159 other countries have adopted the GST Law in some form or other. In many countries, VAT is the substitute for GST, but unlike the Indian VAT system, these countries have a single VAT tax, which fulfills the same purpose as GST. In India, the discussion on GST Law was flagged off in the year 2000, when the then Prime Minister Shri. Atal Bihari Vajpayee brought the issue to the table.

History of GST in India

The idea behind having one consolidated indirect tax to subsume multiple currently existing indirect taxes is to benefit the Indian economy in a number of ways:

1. It will help the country's businesses gain a level playing field.
2. It will put us on par with foreign nations who have a more structured tax system.
3. It will also translate into gains for the end consumer who need not have to pay cascading taxes any more.
4. There will now be a single tax on goods and services.

In addition to the above, The Goods and Services Tax Law aims at streamlining the indirect taxation regime. As mention e: above, GST will subsume all indirect taxes levied on goods and service, including State an; Central level taxes. The GST mechanism is advancement on the VAT system, the idea being that a unified GST Law will create a seamless nationwide market. It is also expected that Goods and Services Tax will improve the collection of taxes as well a; boost the development of Indian economy by removing the indirect tax barriers between states and integrating the country through a uniform tax rate.

Advantages of Goods and Services Tax

The Goods & Service Tax is one of the biggest fiscal reforms in India since Independence. All businesses, small or large, will be impacted by this new indirect tax regime. GST will be levied on both goods and services and will subsume and replace the

current indirect taxes such as excise, VAT, and service tax. Some of the benefits of GST to die Indian economy are listed below

a. Removing cascading tax effect.
b. Higher threshold for registration.
c. Composition scheme for small business.
d. Online simpler procedure under GST.
e. Lesser compliances.
f. Defined treatment for e-commerce.
g. Increased efficiency in logistics.
h. Regulating the unorganized sector.
i. Simplicity at its best.
j. Boosting of revenue.
k. Boosting investment

1. **Removing Cascading Tax Effect**: An important benefit of the introduction of GST is the removal of the cascading tax effect. In simple words, "Cascading Tax Effect" means a tax on tax. Under the previous tax system, the service tax paid on input services cannot be set off against output VAT. Under GST, the input tax credit can be availed smoothly across the spectrum of goods and services, thus reducing the tax burden on the end user and removing cascading effect. Let's take the following example to understand how removing the cascading effect will reduce taxes.

   Under Previous Tax System: A trader buys office supplies for ì 20,000 paying 5% as tax. It charges 15% service tax on services of ì 50,000. Currently, he has to pay ì 50,000 x 15% = ì 7,500 without getting any deduction of ì 1,000 VAT already paid on stationery.

   Under GST (assuming GST= 18%)

	₹
GST on Services of ì 50,000@ 18%	9,000
Less: GST on Office Supplies ì (20,000 x 18%)	3,600
Net GST to Pay	5,400

   Hence, under GST the tax burden is reduced by an amount of ?2,100 (i.e. 7,500 - 5,400). This will be especially beneficial to industries that involve both goods and services (like restaurant business) and pay both VAT & Service Tax under the current regime.

2. **Higher Threshold for Registration:** As per the current VAT structure, any business with a turnover of more than 5 lakh (in most states) is liable to pay VAT (different rates in different states). Similarly, for service tax, service providers with turnover of less than ì 10 lakh are exempted. Under GST this threshold has been increased to T20 lakh thus exempting many small traders and service providers.

3. **Composition Scheme for Small Businesses**: GST also has an optional scheme of lower taxes for small businesses with turnover between ì 20 to 50 lakh. It is called the

composition scheme. It has now been proposed to be increased to 75 lakh. This will bring respite from tax burdens to many small businesses.

4. **Simpler Online Procedure under GST**: The entire GST process - starting from registration to filing returns and payment of GST tax - is online. Startups do not have to run around to tax offices to get various registrations under excise, VAT, service tax, etc.

5. **Lesser Number of Compliances**: Also, the previous tax regime has excise, VAT, and service tax, each of which have their own returns and compliances. GST will unify all these, thereby reducing the number of returns and the time spent for tax compliances. There are about 11 returns under GST, out of which 4 are basic returns, which apply to all taxable persons under GST. There are fears that the number of returns will increase after GST. But the main GSTR-1 will be manually populated. But GSTR-2, GSTR-3, GSTR-4 will be auto-populated.

6. **Defined Treatment for E-commerce**: Many Indian businesses provide goods and services through me Internet. Earlier, there were no specific provisions for treatment of the e-commerce sector. Currently, states have variable VAT laws for this sector. For example, online websites (like Flip kart and Amazon) delivering to Uttar Pradesh have to file a VAT declaration and the registration number of the delivery truck. Tax authorities can sometimes seize goods when there is a failure to produce documents.

   Again, these e-com brands are treated as facilitators or mediators by states like Kerala, Rajastiian, and West Bengal, which do not require them to register for VAT. All these differential treatments and confusing compliances will be removed under GST. For the first time, GST clearly maps out the provisions applicable to the e-commerce sector and since these will apply all over India, there should be no complication regarding inter-state movement of goods anymore.

7. **Increased Efficiency in Logistics**: The logistics industry in India had to maintain multiple warehouses across states to avoid the CST and state entry taxes on inter-state movement. Most of the times, these warehouses were forced to operate below their capacity thus increasing their operating costs. Under GST, these restrictions on inter-state movement of goods will be lessened and the logistics sector might start consolidating warehouses across the country. As an outcome of GST, warehouse operators and e-commerce players have already shown interest in setting up their warehouses at strategic locations such as Nagpur, which is the zero-mile city of India, instead of every other city on their delivery route. Reduction in unnecessary logistics costs will increase profits for businesses involved in supply of goods through transportation.

8. **Regulating the Unorganized Sector**: Certain industries in India like construction and textile are largely unregulated and unorganized. GST has provisions for online compliances and payments, and availing of input credit only when the supplier has accepted the amount, thereby bringing accountability and regulation to these industries.

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9. **Simplicity at its Best**: Goods and Service Tax replaced the existing form of indirect tax in the nation. It will prove a substitute for the 17 indirect laws pertaining to the nation and will subsidize it with the new GST Tax. That shall come across as a simpler term to envision.

10. **Boosting of Revenue**: With the new GST in the nation, there won't be more of an evasion as what is happening with the previous tax laws. Such simpler term of taxation will make more suppliers in a mood to pay the tax amount, which in turn marks the boost in revenue levels.

11. **Boosting Investment**: As per the previous tax laws in India, no input credit on capital goods was allowed. But with the new GST Tax laws, one can avail input tax credit on the capital goods. That way, the investment might surge up quite a bit with an expected 6% increase.

Conclusion

There is no doubt that GST is aimed at increasing the taxpayer base by bringing SMEs and the unorganized sector under its purview. This will make the Indian market more competitive than before and create a level playing field between large & small enterprises. Further, Indian businesses will be able to better compete with foreign countries such as China, Philippines, and Bangladesh.

15. Describe the causes for increase in public debt and explain the methods of redemption of public debt.
பொதுக்கடன் அதிகரிப்பதற்கான காரணங்களை விவரிக்கவும் மற்றும் பொதுக்கடனை மீட்பதற்கான வழிமுறைகளை விளக்கவும்

Public Debt

In the 18th and 19th centuries, the role of the state was minimum. But since 20th century there has been enormous increase in the responsibilities of the state. Hence the state has to supplement the traditional revenue sources with borrowing from individuals, and institutions within and outside the country. The amount of borrowing is huge in the under developed countries to finance development activities. The debt burden is a big problem and most of the countries are in debt trap.

Definitions

"The debt is the form of promises by the Treasury to pay to the holders of these promises a principal sum and in most instances interest on the principal. Borrowing is resorted to in order to provide funds for financing a current deficit."
– Philip E.Taylor

"The receipt from the sale of financial instruments by the government to individuals or firms in the private sector, to induce the private sector to release manpower and real resources and to finance the purchase of these resources or to make welfare payments or subsidies".
– Carl S.Shoup

Causes for the Increase in Public debt

The causes for enormous growth of public debt may be studied under the following sub-headings:

1. War and Preparation of war

Waging war has become one of the important causes for incurring debts by the governments. In modern times, the preparation for war and nuclear defence programmes take away the major share of the government's revenue and so it incurs debt.

2. **Social obligations**

Modern states are considered to be 'Welfare States' and they have to undertake many social obligations like public health, sanitation, education, insurance, transport and communications, etc., besides providing the minimum necessaries of life to the citizens of the country. To finance these, the State has to incur a heavy public debt.

3. Economic Development and Deficit

The government has to undertake many projects for economic development of the country. Construction of railways, power projects, irrigation projects, heavy industries, etc., could be thought of only by means of mobilising resources in the form of public debt. Due to heavy public expenditure, the governments always face deficit budget. Such deficits have to be financed only through borrowings.

4. Employment

Most of the governments of modern days face the problem of unemployment and it has become the duty to solve this by making huge public expenditure. To solve the unemployment problem, and to fight recession, the government has to make huge expenditures. For this the States have to resort to public debt.

5. Controlling inflation

The Government can withdraw excess money from circulation, by raising public debt and thus prevent prices from rising.

6. Fighting depression

During the depression phase, private investment is lacking. The Government applies compensatory public spending by borrowing from internal and external sources.

Methods of Redemption of Public Debt

The process of repaying a public debt is called redemption. The Government sells securities to the public and at the time of maturity, the person who holds the security surrenders it to the Government. The following methods are adopted for debt redemption.

(1). Sinking Fund

Under this method, the Government establishes a separate fund known as "Sinking Fund". The Government credits every year a fixed amount of money to this fund. By the time the debt matures, the fund accumulates enough amount to pay off the principal along with interest. This method was first introduced in England by Walpol.

(2). Conversion

Conversion of loans is another method of redemption of public debt. It means that an old loan is converted into a new loan. Under this system a high interest public debt is converted into a low interest public debt. Dalton felt that debt conversion actually relaxes the debt burden.

(3). Budgetary Surplus

When the Government presents surplus budget, it can be utilised for repaying the debt. Surplus occurs when public revenue exceeds the public expenditure. However, this method is rarely possible.

(4). Terminal Annuity

In this method, Government pays off the public debt on the basis of terminal annuity in equal annual instalments. This is the easiest way of paying off the public debt.

(5). Repudiation

It is the easiest way for the Government to get rid of the burden of payment of a loan. In such cases, the Government does not recognise its obligation to repay the loan. It is certainly not paying off a loan but destroying it. However, in normal case the Government does not do so; if done it will lose its credibility.

(6). Reduction in Rate of Interest

Another method of debt redemption is the compulsory reduction in the rate of interest, during the time of financial crisis.

(7). Capital Levy

When the Government imposes levy on the capital assets owned by an individual or any institution, it is called capital levy. This levy is imposed on capital assets above a minimum limit on a progressive scale. The fund so collected can be used by the Government for paying off war time debt obligations. This is the most controversial method of debt repayment.

16. **What is deficit financing? What are the objectives of deficit financing? Discuss the merits and demerits of deficit financing**
பற்றாக்குறை நிதியாக்கம் என்றால் என்ன? பற்றாக்குறை நிதியாக்கத்தின் நோக்கங்கள் யாவை? பற்றாக்குறை நிதியாக்கத்தின் நன்மை தீமைகள் பற்றி விவாதி

Objectives of Deficit Financing

(1) To accelerate economic development —In the developing economy when the Government fails to mobilize adequate resource for the public sector plan from domestic as well as external resources, recourse to deficit financing becomes necessary. In India, deficit financing performs a new and a far more important function, viz to accelerate economic development.

(2) For economic stability—Deficit financing is used as an instrument of recovery after depression and also to mitigate the severity of the business cycle. Deficit financing has assumed these forms in this context, viz., 'pump priming' and 'cyclical deficit spending'.

(3) For the prosecution of war—Deficit financing becomes necessary during wars when all the resources that the Government can raise in the form of taxes and loans prove insufficient to meet the enormous increase in expenditure.

(4) For the mobilization of idle resources—Deficit financing is also advocated for the mobilization of surplus, idle and unutilized resources the economy

(5) For employment—Deficit financing can have two types of effects on the employment situation

(i) It may bid skilled labour of all kinds away from their present occupations into more productive ones; and

(ii) by offering high enough monetary wages made possible by deficit financing; a substantial amount of rural work-force can be obtained without reducing the production of the agricultural sector. Thus, deficit financing raises the level of output and employment

Evil Effects of Deficit Financing (case against the deficit financing)

(1) inflationary rise in prices—Deficit financing increases the total volume of outlay and, therefore, there will be an increase in the aggregate demand for goods and services.

When, as a result of deficit financing, inflation goes too far, it becomes self-defeating. The rising prices are followed by rising costs and the latter cause further rise in prices, so that a spiral of inflation is set in.

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(2) Fiscal deficit and expansion in public debt and other liabilities. - In the last decade, fiscal deficit was rising very fast and consequently, the public debt and other liabilities of the Government of India were literally multiplying

(3) Forced Savings—When inflation occurs as a result of deficit spending, consumption must decline as a result of rising prices and, therefore, savings become forced

(4) Change in the pattern of investment—Investment caused by inflation may not be of the pattern sought under the plan. There are certain fields of investments which receive strong encouragement from inflation.

(5) Credit creation by banks—Inflationary forces created by deficit financing are reinforced by increased credit creation by banks Increase in Government spending without a corresponding decrease in private spending raises the bank deposits with the Central Bank

The deficit financing can be used for promoting capital formation in the following ways:

(i) The immediate result of deficit financing is to create additional currency or credit. This additional purchasing power enables Government to outbid consumers in the procurement of resources. Thus, resources get diverted from current consumption to capital formation,

(ii) Deficit financing activates idle savings,

(iii) Deficit financing, by increasing incomes, makes far more savings and thus provides a necessary supplement to provide voluntary saving,

(iv) It breaks rigidities and bottlenecks which hold down production,

(v) Through the process of development, monetisation of the economy becomes the cause of increased demand for money, which can be satisfied through deficit financing

17. What is FDI and FPI? Mention the objectives of FDI. Explain the role of FDI in Economic Development of India

அந்நிய நேரடி முதலீடு மற்றும் அந்நிய தொகு முதலீடு என்றால் என்ன? அந்நிய நேரடி முதலீட்டின் நோக்கங்கள் யாவை? இந்திய பொருளாதார வளர்ச்சியில் அந்நிய நேரடி முதலீட்டின் பங்கினை விளக்குக

Meaning of FDI

FDI means an investment in a foreign country that involves some degree of control and participation in management. It corresponds to the investment made by a multinational enterprise in a foreign country. It is different from portfolio investment, which is primarily motivated by short term profit and it does not seek management control.

Objectives of FDI

FDI has the following objectives.

1. Sales Expansion
2. Acquisition of resources
3. Diversification
4. Minimization of competitive risk.

Advantages of FDI

Foreign investment mostly takes the form of direct investment. Hence, we deal here with the foreign direct investment.

The important advantages of foreign direct investment are the following:

1. FDI may help to increase the investment level and thereby the income and employment in the host country.

2. Direct foreign investment may facilitate transfer of technology to the recipient country.

3. FDI may also bring revenue to the government of host country when it taxes profits of foreign firms or gets royalties from concession agreements.

4. A part of profit from direct foreign investment may be ploughed back into the expansion, modernization or development of related industries.

5. It may kindle a managerial revolution in the recipient country through professional management and sophisticated management techniques.

6. Foreign capital may enable the country to increase its exports and reduce import requirements. And thereby ease BoP disequilibrium.

7. Foreign investment may also help increase competition and break domestic monopolies.

8. If FDI adds more value to output in the recipient country than the return on capital from foreign investment, then the social returns are greater than the private returns on foreign investment.

9. By bringing capital and foreign exchange FDI may help in filling the savings gap and the foreign exchange gap in order to achieve the goal of national economic development.

10. Foreign investments may stimulate domestic enterprise to invest in ancillary industries in collaboration with foreign enterprises.

11. Lastly, FDI flowing into a developing country may also encourage its entrepreneurs to invest in the other LDCs. Firms in India have started investing in Nepal, Uganda, Ethiopia and Kenya and other LDCs while they are still borrowing from abroad. Larger FDI to India comes from a small country (Mauritius).

FDI in India

The early 1990s witnessed reforms in the economic policy. This helped to open up Indian markets to FDI. FDI in India has increased over the years. In India, FDI has been advantageous in terms of free flow of capital, improved technology, management expertise and access to international markets.

The major sectors benefited from FDI in India are:

(i) financial sector (banking and non-banking)
(ii) insurance
(iii) telecommunication
(iv) hospitality and tourism
(v) pharmaceuticals and
(vi) software and information technology.

FDI is not permitted in the industrial sectors like

(i) Arms and ammunition
(ii) atomic energy,
(iii) railways,
(iv) coal and lignite and
(v) mining of iron, manganese, chrome, gypsum, sulphur, gold, diamonds, copper etc.,

FDI inflow in India has increased from $97 million in 1990-91 to $5,535 million in 2004-2005. It amounted to $32,955 million in 2011-2012. UNCTAD's World Investment Report 2018 reveals that FDI to India declined to $40 billion in 2017 from $44 billion in 2016.

Role of Foreign Capital in Economic Development

Foreign capital combined with skill and enterprise is essential for the development of under-developed countries in several ways:

1. It is necessary to invite foreign capital when domestic capital is inadequate for the purpose of economic growth.

2. Foreign capital supplements domestic savings and harnesses them to secure a rapid rate of growth.

3. It provides technological expertise and helps in building a modern industrial structure.

4. It paves the way for the investment of domestic capital into new and desirable channels not attempted in the country before for lack of bold entrepreneurship.

5. It provides valuable foreign exchange.

6. It eases pressures on the balance of payments.

7. It can help developing countries in breaking the vicious circle of poverty.

8. During the early stages of economic development of backward countries, the vast natural resources would be exploited quickly with foreign capital.

9. Foreign capital helping to import some of the essential goods of consumption can help contain inflationary pressures in the economy making the process of development relatively easy and smooth.

10. Foreign capital reduces the strain of development on the people of developing countries

18. Explain the causes of BOP Disequilibrium and measures to correct BOP disequilibrium.
செலுத்தல் சமநிலையில் ஏற்படும் சமமற்ற நிலைக்கான காரணங்களை விளக்கி அதனை சரிசெய்ய எடுக்க வேண்டிய நடவடிக்கைகளையும் விளக்குக

Causes for BoP Disequilibrium

The following are the major causes producing disequilibrium in the balance of payments of a country.

1. **Cyclical Fluctuation:** Cyclical disequilibrium in different countries is caused by their cyclical fluctuations, their phases and magnitude. World trade shrinks during depression while trade flourishes during prosperity

2. **Structural Changes:** Structural disequilibrium is caused by the structural changes brought by huge development and investment programmes in the developing economies. Such economies may have high propensity to import for want of capital for rapid industrialization, while export may not be boosted up to that extent.

3. **Development Expenditure:** Development disequilibrium is caused by rapid economic development which results in income and price effects. The less developed countries in the early stage of development are not self sufficient. Income, savings and investment are abysmally low. They depend upon developed countries for import of commodities, capital and technology. Export potential is low and import intensity is high. So the LDCs suffer from adverse BoP.

4. **Consumerism:** Balance of payments position of a country is adversely affected by a huge increase in consumption. This increases the need for imports and decreases the capacity to export.

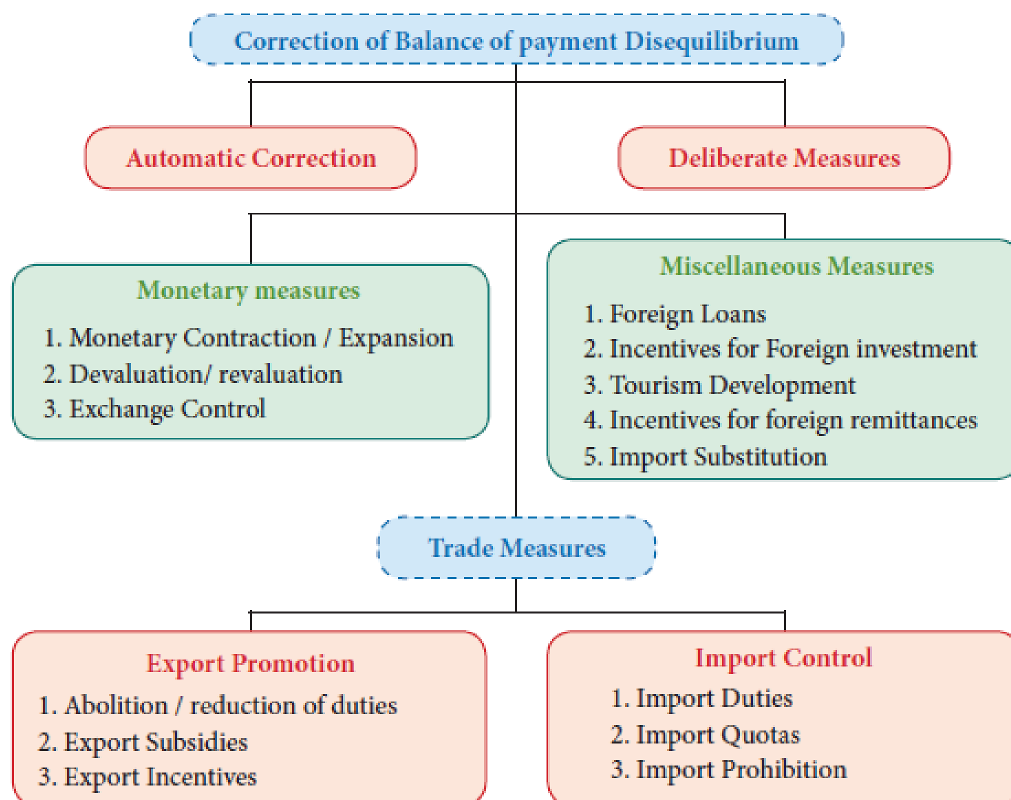
5. **Demonstration Effect:** Deficit in the balance of payments of developing countries is also caused by demonstration effect which influences the people in UDCs to imitate western styled goods. This will raise the propensity to import causing adverse balance of payments. This is good for the developed countries.

6. **Borrowing:** International borrowing and investment may cause a deficit in the balance of payments. When the international borrowing is heavy, a country's balance of payments will be adverse since it repays loans with interest. Servicing of debt is a huge burden. That is why the UDCs are forced to borrow more.

7. **Technological Backwardness:** Due to technological backwardness, the people (Indians) are unable to use the energy (Solar) available with them. As a result they import huge petroleum products from foreign countries, increasing the trade deficit.

8. **Global Politics:** The rich countries (Eg. USA) need to sell their weapons to promote their economy and generate employment. Hence, wars between countries (for example Iran and Irag, Pakistan and India) are stimulated In order to win the wars, the poor countries are forced to buy the weapons from weapon – rich countries, using their export earnings and creating trade deficit. Thus UDCs are trapped forever.

Measures to Correct BOP Disequilibrium



19. Describe the impact of global financial crisis on Indian Economy
இந்திய பொருளாதாரத்தில் உலகளாவிய நிதிச் சிக்கல் ஏற்படுத்திய தாக்கம் பற்றி விவரி.

IMPACT OF GLOBAL ECONOMIC CRISIS ON INDIAN ECONOMY

Offshoot of Globalized Economy

- With the increasing integration of the Indian economy and its financial markets with rest of the world, there is recognition that the country does face some downside risks from these international developments.

- The risks arise mainly from the potential reversal of capital flows on a sustained medium term basis from the projected slow down of the global economy, particularly in advanced economies, and from some elements of potential financial contagion.

(a) Capital Outflow

- The main impact of the global financial turmoil in India has emanated from the significant change experienced in the capital account in 2008-09, relative to the previous year. Total net capital flows fell from US$17.3 billion in April-June 2007 to US$13.2 billion in April-June 2008.

- Nonetheless, capital flows are expected to be more than sufficient to cover the current account deficit this year as well.

(b) Impact on Stock and Forex Market

- With the volatility in portfolio flows having been large during 2007 and 2008, the impact of global financial turmoil has been felt particularly in the equity market. Indian stock prices have been severely affected by foreign institutional investors' (FIIs') withdrawals.

- FIIs had invested over Rs 10,00,000 crore between January 2006 and January 2008, driving the Sensex 20,000 over the period. But from January, 2008 to January, 2009 this year, FIIs pulled out from the equity market partly as a flight to safety and partly to meet their redemption obligations at home.

(c) Impact on the Indian Banking System

- One of the key features of the current financial turmoil has been the lack of perceived contagion being felt by banking systems in emerging economies, particularly in Asia. The Indian banking system also has not experienced any contagion, similar to its peers in the rest of Asia.

- The Indian banking system is not directly exposed to the sub-prime mortgage assets. It has very limited indirect exposure to the US mortgage market, or to the failed institutions or stressed assets. Indian banks, both in the public sector and in the private sector, are financially sound, well capitalized and well regulated.

(d) Impact on Industrial Sector and Export Prospect

- The financial crisis has clearly spilled over to the real world. It has slowed down industrial sector, with industrial growth projected to decline from 8.1 per cent from last year to 4.82 per cent this year.

- The service sector, which contributes more than 50 per cent share in the GDP and is the prime growth engine, is slowing down, besides the transport, communication, trade and hotels & restaurants sub-sectors.

(e) Impact on Employment

- Industry is a large employment intensive sector. Once, industrial sector is adversely affected, it has cascading effect on employment scenario.

- The services sector has been affected because hotel and tourism have significant dependency on high-value foreign tourists. Real estate, construction and transport are also adversely affected.

(f) Impact on poverty

20. Write a short note on the following
பின்வருவனவற்றிற்கு சிறுகுறிப்பு வரைக

a. EXIM Policy 2015-20
ஏற்றுமதி இறக்குமதி கொள்கை 2015-20

Export and Import Policy

The Government of India, Ministry of Commerce and Industry announced New Foreign Trade Policy on 01st April 2015 for the period of 2015-2020.

Salient Features of "EXIM POLICY (2015-2020)"

The new EXIM policy has been formulated focusing on increasing in exports scenario, boosting production and supporting the concepts like Make in India and Digital India.

- Reduce export obligations by 25% and give boost to domestic manufacturing supporting the "Make in India" concept.
- As a step to Digital India concept, online procedure to upload digitally signed document by CA/CS/Cost Accountant are developed and further mobile app for filing tax, stamp duty has been developed.
- Repeated submission of physical copies of documents available on Exporter Importer Profile is not required.
- Export obligation period for export items related to defence, military store, aerospace and nuclear energy to be 24 months.
- EXIM Policy 2015-2020 is expected to double the share of India in World Trade from present level of 3% by the year 2020. This appears to be too ambitions.

b. Non Performing Assets (NPA)
வாராக் கடன்

Non-Performing asset

The assets of the banks which don't perform (that is – don't bring any return) are called **Non-Performing Assets (NPA**) or bad loans. According to RBI, terms loans on which interest or installment of principal remain overdue for a period of more than **90 days** from the end of a particular quarter is called a **Non-performing Asset**.

SARFAESI Act, 2002

Government of India finally cracked down on the wilful defaulters by passing the **Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002.**

Once the borrower fails to make interest or principal payments for 90 days the loan is considered to be a non- performing asset (NPA). NPAs are problematic for financial institutions since they depend on interest payments for income. As on now the size of NPAs is estimated to be around 10 lakh crores. As a result, the banks do not have adequate capital. Hence the Government (of India) is forced to infuse capital to the banks by using poor tax – payers money. Already more than a sum of ₹ 2 lakh crores have been injected. During 2018 - 19, the GOI has infused 68,000 crores into the banking system. Thus the NPAs ultimately affect the common people.

c. FOREX Market
வெளிநாட்டு பரிமாற்றச் சந்தை

Meaning of Foreign Exchange (FOREX)

FOREX refers to foreign currencies. The mechanism through which payments are effected between two countries having different currency systems is called FOREX system . It covers methods of payment, rules and regulations of payment and the institutions facilitating such payments.

Definition of FOREX

"FOREX is the system or process of converting one national currency into another, and of transferring money from one country to another".

Rate of Exchange

The transactions in the exchange market are carried out at exchange rates. It is the external value of domestic currency. Thus, exchange rate may be defined as the price paid in the home currency (say ₹ 75) for a unit of foreign currency (say 1 US $). It can be quoted in two ways:

1. One unit of foreign money (1 USD) to so many units of the domestic currency (₹); or
2. A certain number of units of foreign currency (USD) to one unit of domestic money (₹ 1)

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